

**CITY OF BLAINE**  
**Whatcom County, Washington**  
**January 1, 1994 Through December 31, 1994**

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**Schedule Of Findings**

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1. The City Should Only Pay For Services Which Have Been Rendered And Which Are Allowable City Expenditures

Our review of the city's expenditures revealed payments which were either paid in advance, not allowable expenditures for a city, or could be construed as gifts of public funds. We noted the following:

- a. Payments totaling in excess of \$25,000 were made in advance of services provided to a private nonprofit service organization for fiscal years 1995 and 1994 without an agreement or contract detailing what services were to be provided. The city was unable to provide documentation of what services had actually been provided. This occurred even though the city's lease agreement with this organization states the city is:

Not required to contribute financially . . . or otherwise  
subsidize . . . .

- b. Payments totaling \$1,500 were made to a private organization for fiscal year 1994 without an agreement or contract detailing what services were to be provided. The city was unable to provide documentation of what services had actually been provided.

- c. Payments totaling \$1,800 were made to a private organization for fiscal years 1995 and 1994 without adequate documentation of what services had actually been provided. The city's agreement with the organization states:

The claim shall be supported by detailed documentation of the  
services performed . . . .

- d. Reimbursement payments made to a private organization totaling \$190 for expenditures which are not allowable city expenditures. Payments included reimbursement for flowers and alcoholic beverages distributed as gifts.

RCW 43.09.200 states in part:

The accounts shall show the receipt, use, disposition of all public property, and the income, if any, derived therefrom; all sources of public income, and the amounts due and received from each source; all receipts, vouchers, and other documents kept, or required to be kept, necessary to isolate and prove the validity of every transaction . . . .

In addition, RCW 42.24.080 states in part:

All claims presented against any county, city, district or other municipal corporation or political subdivision by persons furnishing materials, rendering services or performing labor or for any other contractual purpose, shall be audited, before payment, by an auditing officer elected or appointed pursuant to statute . . . Such claims shall be prepared for audit and payment on a form and in the manner prescribed by the state auditor. The form shall provide for the authentication and certification by such auditing officer that the materials have been furnished, the services rendered or the labor performed as described, and that the claim is just, due and unpaid obligation against the municipal corporation or political subdivision; and no claim shall be paid without such authentication and certification . . . (Emphasis ours.)

Further, Article VIII, Section 7 of the Washington State Constitution states in part:

No county, city, town or other municipal corporation shall hereafter give any money, or property, or loan its money, or credit to or in aid of any individual, association, company or corporation, except for the necessary support of the poor or infirm . . .

The city officials were not aware of applicable laws and did not develop procedures to ensure all goods and services have been received prior to payment and all expenditures are for allowable city purposes. As a result, the city reimbursed expenditures which were made for improper purposes. Further, goods and services may not have been provided or performed as the city intended. Also, by paying for goods and services prior to them being provided, the city has limited its recourse in the event of damaged goods, nonperformance of services or a change of plans. In addition, lack of documentation and improper expenditures could be construed as gifts of public funds to the organizations.

We recommend the city improve controls over expenditures as follows:

- a. Develop adequate agreements with all organizations to ensure services are allowable city expenditures.
- b. Require adequate supporting documentation detailing the services provided and ensuring it is received prior to payment for the services.
- c. Ask for and receive adequate documentation for past payments to these organizations or request reimbursement for those payments.
- d. Review all expenditures to ensure expenditures are not gifts of public funds.

2. The City Should Report And Account For The Water/Wastewater Utility Based Upon Generally Accepted Accounting Principles (GAAP)

The City of Blaine reported and accounted for the Water/Wastewater Utility Fund on a cash basis of accounting. We noted the total operating revenues for the Water/Wastewater Utility Fund were \$2,123,136 for fiscal year 1994. The fund should have been accounted for on the full accrual basis of accounting.

RCW 43.09.200, states in part:

The state auditor shall formulate, prescribe, and install a system of accounting and reporting, for all local governments, which shall be uniform for every public institution, and every public office, and every public account of the same class.

The *Budgeting, Accounting, and Reporting System (BARS)* manual, as promulgated by the State Auditor, prescribes that:

Cities that are classified as Category 2 must employ double-entry accounting for all internal service funds and for any enterprise funds that have operating revenues of \$2,000,000 or more.

Generally accepted accounting principles (GAAP) requires revenue and expenditure recognition on the full accrual basis of accounting for proprietary funds. The National Council on Governmental Accounting (NCGA) Statement 1, *Governmental Accounting and Financial Reporting Principles* in Paragraph 18, Subparagraph (2) states:

The generally accepted accounting principles here are those applicable to similar businesses in the private sector; and the measurement focus is upon determination of *net income, financial position, and changes in financial position*.

Paragraph 57, subparagraph 8.b. further states:

*Proprietary fund* revenues and expenses should be recognized on the accrual basis. Revenues should be recognized in the accounting period in which they are earned and become measurable; expenses should be recognized in the period incurred, if measurable.

The city had not allocated sufficient resources to meet the additional reporting requirements and continued to account and report the Water/Wastewater Utility financial transactions on a cash basis for fiscal year 1994.

We consider the condition reported here to be a material noncompliance with the laws of the state of Washington.

By not preparing financial statements at the level required by the BARS manual, information used to compile local governmental statistics for the legislature is incomplete. Furthermore, readers of the financial statements may be misled with the information presented on a non-GAAP basis and comparability of financial data between the City of Blaine Water/Wastewater Utility and other utilities of similar nature and size.

We recommend the City of Blaine prepare its future Water/Wastewater Utility financial statements according to generally accepted accounting principles, as prescribed by the

BARS manual.

3. The City Should Improve Controls Over Public Works Materials And Supplies Inventory

During a review of the public works materials and supplies inventories during a special audit of 1991 and 1992, we noted several weaknesses in the inventory control system. Our fiscal year 1993 audit revealed the city had made improvements in some areas, but has not yet addressed some critical concerns. Our current audit revealed no significant improvement in the following areas:

- a. There are no written policies and procedures relating to the access to, issuance of, and accounting for inventory items.
- b. Responsibility for inventory has been fixed, but proper safeguards over inventory are not in place.
- c. The current system does not ensure that supplies and materials are charged at the correct prices to projects and does not provide accurate information with which to determine if loss or theft of inventory has occurred.
- d. Reconciliations are not performed which would allow management to monitor the effectiveness of the controls implemented and identify weaknesses in the system.

RCW 43.09.200, states in part:

The accounts shall show the receipt, use and disposition of all public property, and the income, if any, derived therefrom; all sources of public income, and the amounts due and received from each source: all receipts, vouchers, and other documents kept or required to be kept, necessary to isolate and prove the validity of every transaction . . . . (Emphasis added.)

The American Institute of Certified Public Accountants (AICPA) in its *Codification of Statements on Auditing Standards*, AU Section 319, Appendix D, states in part:

Establishing and maintaining an internal control structure is an important management responsibility. In establishing specific internal control structure policies and procedures concerning an entity's ability to record, process, summarize and report financial data that is consistent with management's assertions embodied in the financial statements, some of the specific objectives management may wish to consider include the following:

- Transactions are executed in accordance with management's general or specific authorization.
- Transactions are recorded as necessary (1) to permit preparation of financial statements in conformity with generally accepted accounting principles or any other criteria to such statements and (2) to maintain accountability of assets.
- Access to assets is permitted only in accordance with management's authorization.
- The recorded accountability for assets is compared with existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

### Access to Assets

The objective of safeguarding assets requires that access be limited to authorized personnel. In this context, access to assets includes both direct physical and indirect access through the preparation or processing of documents that authorize the use or disposition of assets. Access to assets is required in the normal operations of a business and, therefore, limiting access to authorized personnel is the maximum feasible constraint. The number and competence of personnel to whom access is authorized should be influenced by the nature of the assets and the related susceptibility to loss through errors and irregularities. Limitation of direct access to assets requires appropriate physical segregation and protective equipment or devices. (Emphasis added.)

Management has not implemented basic system controls, making it difficult to hold individuals responsible or accountable for their own activities. As a result, inventory is not adequately safeguarded to discourage theft and other irregularities or to discover those occurrences in a timely manner. In addition, accounting records cannot be relied upon to determine the accurate costs of inventory, costs charged to projects, or to support the preparation of financial statements.

We recommend the city improve controls over inventory as follows:

- a. Continue to develop comprehensive written policies and procedures relating to access to, issuance of, and accounting for inventory items.
- b. Provide individuals who have the responsibility for inventory the ability necessary to control access to inventory.
- c. Establish basic inventory accounting procedures to control the issuance, return, and use of inventory and to ensure the proper pricing of supplies and materials to projects performed.
- d. Perform timely reconciliations of inventory supply and charges to other funds to help monitor the effectiveness of the controls implemented.

4. The City Public Works Department's Work Order System Needs To Be Strengthened And Implemented Department Wide

During our review of the city's work order system, as part of a special audit covering 1991 and 1992, we noted several weaknesses. A follow up, performed during the 1993 fiscal year audit, revealed improvements had been made in implementing one system for all of public works and ensuring all work orders are processed in a more timely manner. During the current audit we noted the following weaknesses still exist:

- a. There is a lack of written policies and procedures relating to work orders.
- b. The current computerized work order system does not interface with the current accounting software.
- c. Procedures are inadequate to ensure all materials, time, and vehicles usage are charged on work orders or that all charges to the work order system are supported by payroll reports.
- d. Fixed asset usage rates lack supporting documentation. (See Federal Finding 1).

RCW 39.04.070, states:

Whenever the state or any municipality shall execute any public work by any means or method other than by contract or small works roster, it shall cause to be kept and preserved a full, true and accurate account and record of the costs of executing such work in accordance with the budgeting, accounting, and reporting system provisions prescribed by law for the state agency . . . (Emphasis added.)

Management has not implemented basic accounting systems to provide accurate accounting for work performed. As a result, the city cannot ensure all costs are charged or support all charges to projects. In addition, with the condition of the fixed asset system, as noted in Federal Finding 1, the city cannot ensure accurate costs are charged with respect to vehicle rental rates. Furthermore, accounting records cannot be relied upon to determine the actual costs charged to projects or to support the preparation of financial statements.

We recommend the city implement an adequate work order control system.

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**Schedule Of Federal Findings**

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1. The City Should Improve Its Accounting For Fixed Assets

As noted in prior audit reports, the city's controls over fixed assets are inadequate. We noted the city's public works department has begun to implement a fixed asset physical inventory, but has not fully implemented a fixed asset detail ledger. The other funds have not taken a comprehensive annual physical inventory or implemented a comprehensive fixed asset detail ledger.

Because of the absence of adequate accounting procedures and controls, the city is not properly safeguarding public fixed assets. Furthermore, the city does not have adequate information to:

- a. Fix responsibility for custody of its assets.
- b. Provide adequate insurance coverage.
- c. Determine proper depreciation expense for the proprietary funds.
- d. Plan an effective replacement and maintenance program.
- e. Identify fixed assets acquired with federal funds and the final disposition of such property.

RCW 43.09.200 states in part:

The accounts shall show the receipt, use, and disposition of all public property . . . .

RCW 43.09.200 also requires the State Auditor to prescribe the uniform accounting systems. The State Auditor prescribes the *Budgeting, Accounting, and Reporting System* (BARS) manual which states, in Volume 1, Part 3, Chapter 7, page 7:

Accountability for fixed assets is required of all local governments, regardless of size.

The Light Utility Fund uses the Federal Energy Regulatory Commission's (FERC) *Uniform System of Accounts for Public Utilities and Licensees* prescribed by the State Auditor in accordance with RCW 43.09.200. General instruction No. 2(a) in this prescribed system of accounts states that:

Each utility shall keep its book of accounts, and all other books, records, and memoranda which support the entries in such book of accounts as



to any item included in any account.

Additionally, for any fixed assets purchased by the city using federal funds, the Office of Management and Budget (OMB) "Common Rule," section .32, [d] Management requirements, states in part:

- (1) Property records must be maintained that include a description of the property, who holds title, the acquisition date, and cost of the property, percentage of Federal participation in the cost of the property, the location, use and condition of the property, and any ultimate disposition data including the date of disposal and sale price of the property.
- (2) A physical inventory of the property must be taken and the results reconciled with the property records at least once every two years.
- (3) A control system must be developed to ensure adequate safeguards to prevent loss, damage, or theft of the property. Any loss, damage, or theft should be investigated.

Furthermore, generally accepted accounting principles require accounting for fixed assets and related depreciation.

In previous years, city officials were reluctant to allocate the financial resources necessary to establish an adequate system of accounting for its fixed assets. In 1990, the city contracted with an appraisal company to inventory and appraise the utility funds' fixed assets, however, the data obtained from the appraisal was not utilized promptly to update the fixed asset records. The public works department has recently initiated the process of performing a physical inventory of fixed assets and implementing a system to record and track those assets.

We consider the conditions reported above to be a material weakness in the internal control structure.

Because the city does not account for its fixed assets, there is an increased risk that errors or irregularities may occur and not be detected in a timely manner, if at all. In addition, we are unable to verify the accuracy of fixed assets, accumulated depreciation, and depreciation expense as presented in the financial statements of the Light utility.

We again recommend city officials continue their efforts to establish a fixed asset accounting system and conduct annual physical inventories of fixed assets.